229219

GKG Law, P.C.

RICHARD BAR
BRENDAN COLLINS
STEVEN JOHN FELLMAN
EDWARD D. GREENBERG
KATHARINE FOSTER MEYER
DAVID K. MONROE
TROY A. ROLF
DAVID P. STREET
KEITH G. SWIRSKY
THOMAS W. WILCOX
CHRISTOPHER B. YOUNGER •

SVETLANA V. LYUBCHENKO

ROBERT N. KHARASCH°

° OF COUNSEL
• NOT ADMITTED IN DC

MINNESOTA OFFICE:
700 TWELVE OAKS CENTER DRIVE, SUITE 700
WAYZATA, MN 55391
TELEPHONE: 952.449.8817 FACSIMILE: 952.449.0614

WRITER'S DIRECT E-MAIL ADDRESS
TWILCOX@GKGLAW.COM

WRITER'S DIRECT DIAL NUMBER
202-342-5248

April 12, 2011

Ms. Cynthia T. Brown
Chief, Section of Administration
Office of Proceedings
Surface Transportation Board
395 E Street, SW
Washington, DC 20423

ENTERED
Office of Proceedings
APR 12 2011
Part of
Public Record

Re: STB Docket No. EP 705, *Competition in the Railroad Industry*

Dear Ms. Brown:

Enclosed for e-filing in the above-captioned proceeding please find the Joint Initial Comments of Omaha Public Power District, The AES Corporation, Oklahoma Gas & Electric Co. and Colorado Springs Utilities.

Please feel free to contact me if you have any questions.

Sincerely,

Thomas W. Wilcox

Thomas W. Wilcox
Counsel for Omaha Public Power District; The AES Corporation; Oklahoma Gas & Electric Co.; and Colorado Springs Utilities

TWW/swf
Enclosure

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Docket No. EP 705

COMPETITION IN THE RAILROAD INDUSTRY

JOINT INITIAL COMMENTS OF OMAHA PUBLIC POWER DISTRICT, THE AES CORPORATION, OKLAHOMA GAS & ELECTRIC COMPANY, AND COLORADO SPRINGS UTILITIES

Pursuant to the procedural schedule issued in this proceeding on February 4, 2011, Omaha Public Power District ("OPPD"), The AES Corporation ("AES"), Oklahoma Gas & Electric Company ("OG&E"), and Colorado Springs Utilities ("CSU") (together "Utilities") hereby jointly submit initial comments in this proceeding. The Utilities commend the Surface Transportation Board ("STB" or "Board") for commencing this important and timely proceeding to receive comments and evidence to explore the current state of competition in the railroad industry and possible policy alternatives to facilitate more rail-to-rail competition, where appropriate. In these Initial Comments, the Utilities provide the Board with comments on the current lack of effective competition between railroads for the transportation of coal to coal fired electrical generating stations, and suggest several policy alternatives for the Board's consideration.

I. Description of the Utilities

A. Omaha Public Power District

OPPD is a public corporation and political subdivision of the State of Nebraska with its principal place of business in Omaha, Nebraska. OPPD provides electrical service to more than 340,000 residential, commercial, industrial, and governmental customers in a 13-county territory in eastern and southeastern Nebraska that includes the Omaha metropolitan area. OPPD generates electricity to serve its customers from a mix of generating resources that include the North Omaha Power Station ("NOPS"), a 646-megawatt-capacity plant located in Omaha, Nebraska, and the Nebraska City Power Station ("NCPS"), a 1330-megawatt-capacity plant located south of Nebraska City, Nebraska. Both plants burn Wyoming Powder River Basin ("PRB") coal to produce electricity for OPPD's customers. Both plants have direct access to the Union Pacific Railroad Company ("UP") and the BNSF Railway ("BNSF").[1]

B. The AES Corporation

The AES Corporation is a holding company with headquarters in Arlington, Virginia. It is a global power company with subsidiaries throughout the world. The AES Corporation, through it subsidiaries, operates approximately 20 generating facilities in the United States. Five of the facilities are coal-fired generating stations served by Class I railroads. Coal is delivered in single and joint-line service by BNSF, Norfolk Southern Railway Company ("NS"), CSX Transportation Company ("CSXT") and the Kansas City Southern Railroad ("KCS").

---

[1] BNSF accesses NOPS via a five mile switch movement over UP's track.

C. Oklahoma Gas & Electric Company

OG&E is an investor-owned, regulated electric utility and a subsidiary of OG&E Energy Corp, with headquarters in Oklahoma City, Oklahoma. OG&E has a total of 6,800 megawatts of capacity and is engaged in the generation, transmission, and distribution of electric power to more than 765,000 retail customers in Oklahoma and Western Arkansas. OG&E also engages in electric power sales to the wholesale electric market. OG&E owns and operates the Sooner and Muskogee Stations, coal-fired electric generating stations that consume roughly nine million tons of PRB coal per year. Both facilities are base-load power generation sources for OG&E, producing 16 million megawatt hours annually. The Muskogee Station is captive to UP for rail service. The Sooner Station is captive to BNSF, but could potentially also be served by UP under circumstances that would entail the construction of a track and the implementation and exercise of certain trackage rights, as described in more detail below.

D. Colorado Springs Utilities

CSU is a publicly owned electric utility located in Colorado Springs, Colorado. It owns and operates the Martin Drake and Ray Nixon power stations which are both located in the vicinity of Colorado Springs. Both plants burn PRB and Colorado coal. The Drake plant is captive to UP. The Nixon plant is capable of being served by both UP and BNSF, both of which have direct physical access to the facility.

II. Initial Comments on the Current State of Competition in the Railroad Industry

A. Background to This Proceeding

In the decision served in this proceeding on January 11, 2011 ("January 11 Decision"), the STB asked for comments and will hold a public hearing to explore the current state of competition in the rail industry and possible policy alternatives to facilitate more competition, where appropriate.[2] This proceeding follows an attempt by the Board in April of 2009 to examine this same subject in Ex Parte No. 688, *Policy Alternatives to Increase Competition in the Railroad Industry* (served April 14, 2009). That proceeding was terminated immediately after it was started at the request of members of Congress.[3]

This proceeding also was preceded by several other relatively recent reviews of rail competition, commencing with an October, 2006 General Accountability Office report entitled *Freight Railroads, Industry Health has Improved, but Concerns about Competition and Capacity Should be Addressed* ("GAO Report"). The GAO Report examined industry data through 2004, a year which is generally considered just prior to the start of the so-called "railroad renaissance" when Class I railroad rates and revenues dramatically increased between 2005 and 2009. Nevertheless, even based on pre-2005 data, the GAO Report expressed concern over the state of competition in the railroad industry at that time and concluded "[u]ltimately, our analysis suggests a reasonable possibility that shippers in selected markets may be paying excessive rates, and an assessment of competition would determine if this situation reflects reasonable economic practices by the railroads in an environment of excess demand or an abuse of market power."[4] The GAO Report recommended that the STB conduct a more "rigorous analysis of competitive markets to identify the state of competition nationwide, inquire into pricing practices in specific markets, and consider appropriate actions available to

---

2 January 11 Decision at 1.

3 Ex Parte No 688, *Policy Alternatives to Increase Competition in the Railroad Industry*, (served April 17, 2009).

4 GAO Report at 4.

address problems associated with the potential abuse of market power."[5] The STB initially disagreed with this recommendation and declined to undertake "another prolonged national study" due to "pending initiatives" at the STB on rail rate rules and practices.[6] The Board eventually complied with GAO's request and commissioned a study on railroad competition prepared by Laurits R. Christensen Associates, Inc., entitled *A Study of Competition in the U.S. Freight Railroad Industry and Analysis of Proposals that Might Enhance Competition* ("Christensen Study"). The Christensen Study was issued in November, 2009, and then updated in January, 2010. Subsequently, in April, 2010, the state of rail competition also was examined by the United States Department of Agriculture and United States Department of Transportation in a *Study of Rural Transportation Issues* published pursuant to Section 6206 of the Food, Conservation, and Energy Act of 2008 (P.L. 110-246) ("USDA/USDOT Study"). Commentary on the state of rail competition has also recently been provided by the Director of the Economic Analysis Group of the Department of Justice's Antitrust Division.[7]

All of these reports and comments recognize a fundamental fact of the railroad industry that has significantly affected rail-to-rail competition in various commodity markets: the consolidation of the railroad industry into essentially two regional duopolies in the eastern and western United States. The impact of rail industry consolidation was recognized in the USDA/USDOT Study, which states in part, "The rapid consolidation of

---

5 *Id* at 5.

6 S*ee id.* at 80-81 (comments of STB on draft GAO Report).

7 See, Pittman, Russell, *The Economics of Railroad "Captive Shipper" Legislation*, Journal of Transportation Law, Logistics and Policy (Volume 77, No. 3, First Quarter 2010) at 221 ("Pittman"). The views in the article are the author's, not necessarily the Department of Justice's.

the railroad industry through mergers has resulted in a decrease in the unrestricted interchange of traffic, routing choices, and the level of competition among railroads. Shippers are concerned with switching limitations, restricted interchange, paper barriers, inconsistent service, high rates, excessive fuel surcharges, bottleneck rates, and the effectiveness of the rate challenge process."[8] Moreover, USDA and USDOT observed that "the loss of rail-to-rail competition due to railroad mergers and the associated increase in market power was not foreseen by many when the Staggers Act was passed."[9] Finally, the Director of the Department of Justice's Economic Analysis Group recently opined,

> One reason for the current market power enjoyed by the U.S. Class I railroads is the past mergers that have already been allowed by the STB- some of which, as noted above, were either opposed by the Antitrust Division or recommended only with more stringent conditions than were imposed by the STB. The result of these mergers has been two mammoth regional duopolies in which neither duopolist aggressively seeks to poach business from the other. Thus, had antitrust jurisdiction rested with the Antitrust Division at the time the mergers were proposed, the industry likely would be more competitive today.

Pittman at 232.

B. <u>The Facts Confirm a Present Lack of Effective Competition for Coal Transportation</u>

The Utilities submitting this Opening Statement have experienced first hand the absence of effective, meaningful competition between the Class I railroads for their coal transportation and/or a deterioration in rail service. Although a complete dissertation of the relevant facts cannot be made due to contractual confidentiality restrictions, a brief summary is provided for each utility below.

---

8 USDA/USDOT Study at vi.

9 *Id.* at viii.

1. **Omaha Public Power District**

OPPD's NOPS and NCPS plants currently burn around 7 million tons of PRB coal per year. The plants began commercial operation in 1954 and 1979, respectively, and so were initially captive to the Burlington Northern Railroad Company ("BN") for service from the PRB, as BN was the only railroad with access to PRB mines. After the introduction of a predecessor to UP to the PRB in 1984, OPPD invested a considerable amount of resources to establish physical access to UP at NCPS for the purpose of lowering OPPD's rail costs through competition between UP and BN. These efforts included (1) obtaining authority from the Interstate Commerce Commission ("ICC") to construct a common carrier line of railroad connecting NCPS to UP; (2) seeking authority from the ICC under 49 U.S.C. §10901(d) to cross the existing track of the BNSF at NCPS over BNSF's objection; and (3) eventually purchasing from BN in 1997 its 56.75 mile long common carrier line of railroad extending from Collegeview, Nebraska to NCPS, which OPPD currently owns and maintains.[10]

OPPD's efforts paid huge dividends. In 1998, intense competitive bidding by BNSF and UP resulted in OPPD's rail transportation costs being reduced $60 million between 1998 and 2003 (Exhibit 1), and service being provided by BNSF. In 2003, OPPD repeated its competitive bidding process, which resulted in OPPD awarding the business to UP for five years and further lowering its fuel costs in part because UP submitted a competitive contract rate and service terms proposal which was below

[10] Finance Docket No 32630, *Omaha Public Power District – Construction Exemption – in Otoe County, NE, (served May 2, 1995)*; Finance Docket No 32630 Sub No. 1, *Petition under 49 U.S.C. §10901(d)* (served November 5, 1995), and Finance Docket No. 33447, *Omaha Public Power District – Acquisition Exemption – Line of the Burlington Northern and Santa Fe Railway Company*, (served September 12, 1997).

BNSF's (Exhibit 2). The rates under the 2003 contract were well below 180% of UP's variable costs of providing the service. The competition between UP and BNSF also resulted in a lengthy, detailed transportation contract that contained provisions favorable to OPPD, including:

1. An agreement by UP to cycle OPPD's coal trains to and from the PRB mines within a specified number of hours, subject to either a payment by UP to OPPD, or the delivery of sufficient coal volumes to make up the coal UP had failed to deliver in the specified time;

2. A rate adjustment provision based on a percentage of the STB's Rail Cost Adjustment Factor, and a specific agreement by UP that the rail rates would not be subject to a fuel surcharge; and

3. Extensive provisions concerning the supply, operation and maintenance of rail cars supplied by OPPD.

As the expiration date of the 2003 Contract with UP approached in 2008, OPPD pursued exactly the same request for proposal process it had followed in the previous two cycles. However, the responses of the two railroads and the final contract terms and conditions were quite different. For example, the base rates proposed by both UP and BNSF were 90-110% above the expiring contract rates, and were both well above 180% of the railroads' variable costs of providing the service. Moreover, BNSF declined to offer a rail transportation contract proposal at all, insisting instead that OPPD agree to ship pursuant to a "Pricing Authority." Neither railroad would agree to a measurable, enforceable transportation service standard. Finally, both railroads sought to impose a fuel surcharge on their offered rates. At the conclusion of the contracting process, OPPD selected the lesser of two evils and executed a new contract with UP that, combined with coal supply contracts, increased the delivered fuel costs for NOPS and NCPS over $100 million per year over 2008 levels. As a direct result, OPPD was required to raise residential and industrial electricity rates an average of 11% and 27% per month, respectively. (Exhibit C).

2. The AES Corporation

AES's coal-fired plants have experienced significant increases in rail transportation costs since 2004, which AES attributes to a lack of competition in the rail industry. The lack of rail options or an effective regulatory backstop to the exercise of monopoly power by railroads has also resulted in a significant rise in cost and degradation of service that has adversely affected AES's coal-fired plants. Several examples of the effects of the lack of competition in the rail industry on AES include the following.

a. AES Shady Point.

AES's Shady Point plant is located in Bonanza, Oklahoma, and it is captive to the KCS at destination, but both UP and BNSF are capable of making deliveries from western PRB coal mines to their respective interchanges with KCS in Kansas City, Missouri. Such segments are approximately 800 miles of the overall 1100-mile movements, which should provide an opportunity for AES Shady Point to try and lower the overall rate from the PRB to the plant through competition between UP and BNSF for the right to haul coal to the KCS interchange. Additionally the plant also is capable of burning coal from the Illinois basin, which can be delivered by UP and KCS. The plant burns approximately 1,000,000 tons of coal per year. Prior to 2010, coal moved to the plant via a rail transportation contract between BNSF, KCS, and AES Shady Point entered into in 2005. The initial proposal by BNSF and KCS to replace that contract in 2011 exceeded the expiring contract levels by nearly 100%. The significant rate increases proposed by BNSF and KCS provided UP with a clear opportunity to secure the Shady Point coal volumes by offering competitive rates for its portion of the overall movement from the PRB, or as part of a joint proposal with KCS. Unfortunately, UP did not submit a competitive proposal. As a direct result of the lack of rail competitive options, the prior contract was replaced with a new contract with BNSF and KCS that significantly increased the rail rates to this plant and imposed surcharges and other contractual provisions that make the current contract much less favorable to AES Shady Point than the prior contract.

b. AES Eastern Energy

AES Eastern Energy owns and/or operates four plants in the State of New York: AES Somerset, which is captive to CSX, and AES Westover, Greenidge and Cayuga, all three of which are captive to NS. All four of these plants have suffered from a lack of competition in the rail industry and the lack of a sufficient regulatory backstop in the form of potential rate relief or the possibility of alternative rail service. Specifically, rail transportation rates and fuel surcharges to these plants have consistently been well in excess of 180% of the railroads' variable costs of providing service, and the rail transportation costs have threatened the long term viability of these plants. Moreover, over the past five months rail service has degraded considerably to all four plants, but the lack of rail alternatives to maintain coal supplies at adequate levels has led to AES filing several Electric Emergency Incident and Disturbance Reports with the United States Department of Energy, notifying it that the plant coal supplies were reaching dangerously low levels.

3. Oklahoma Gas & Electric Company

OG&E's Sooner and Muskogee Generation Stations together annually burn approximately 9 million tons of PRB coal. The Muskogee Station is captive to UP, and the rates charged by UP for transportation to that facility were recently prescribed by the Board.[11] The Sooner Station was originally captive to the Atchison, Topeka & Santa Fe Railway Company ("ATSF") and since the merger of BN and ATSF into BNSF in 1995 has been physically captive to BNSF. Competition between BN and UP for the origin segment of the movement from PRB mines to Topeka, Kansas, resulted in transportation to Sooner between 1994 and 2009 being provided via a joint line contract movement involving transportation by UP to Topeka, Kansas, and by ATSF to the plant. In addition to competition between UP and BN "above the bottleneck," the presence of a potential 13-mile build-out from Sooner to a line owned by BN pre-merger resulted in rate concessions from ATSF for the destination portion of the movement. In 1993, the build-out threat resulted in a long term contract with ATSF "containing much lower rates than previously available, and with a very favorable (to the utility) escalation mechanism."[12] The preservation of this competitive build-out option was one of the conditions placed by the ICC on its approval of the BN/ATSF merger. Because OG&E demonstrated that "[t]he negotiating leverage provided by the build-out option will disappear with the merger,"[13] the ICC "crafted a condition" it determined would preserve the competitive status quo that required the merger applicants to provide a third carrier – in this case UP –

---

[11] Docket NOR 42111, *Oklahoma Gas & Electric Company v. Union Pacific Railroad Company* (served July 24, 2009).

[12] See *Burlington Northern et al – Merger – Santa Fe Pacific et al*, 10 I.C.C. 2nd 661, 744 (1995).

[13] *Id.* at 745.

with trackage rights over the BNSF track to the point where the build-out could connect to the former BN track.[14] Between 1994 and 2008 OG&E enjoyed the benefit of low rates established through meaningful competition between several Class I railroads over different segments of its overall movements.

Unfortunately, OG&E found a very different rail transportation market when it came time to renew its rail transportation arrangements at Sooner. In the first place, whereas prior to the UP/SP and BN/ATSF mergers UP and BNSF's predecessors had competed for the rights to transport OG&E's coal over the "non-bottleneck" segments of tracks from the PRB to interchange points of ATSF's "bottleneck" segment to Sooner (and also to UP's "bottleneck" segment to Muskogee), this was no longer the case in 2008.

Second, unlike 1993, the presence of potential access to another railroad via the build-out/trackage rights merger condition did not result in BNSF offering lower rates to Sooner in 2008 as the prior contract was due to expire. On the contrary, BNSF offered rates that were more than double the expiring contract rates, and in excess of 180% of BNSF's variable costs of providing service. For its part, UP declined to provide any rate proposals in the absence of having physical access to the Sooner Station. Instead, UP asked OG&E to submit a proposal to UP, which OG&E prepared and submitted, but to which UP never formally responded. In the absence of a competing proposal from UP, OG&E executed a contract with BNSF.

---

[14] *Id.* The implementation of this condition was a grant by BNSF of trackage rights to UP over BNSF's track between Claremore, Oklahoma and Morrison, Oklahoma. In 1996, UP and BNSF entered into an Agreement memorializing the grant of trackage rights and associated terms and conditions, which include steps the parties must take to implement the rights.

4. **Colorado Springs Utilities**

From 2000 to mid-2010 CSU operated under a long term coal transportation contract with UP, by which UP delivered coal from mines in Colorado and Wyoming to both the Drake and Nixon plants. This contract was arrived at through a competitive bidding process with UP and BN, which could then and can today deliver PRB coal directly to the Nixon plant. Part of the agreement with UP that resulted from the bidding process entailed the construction by CSU of a rail spur from the Nixon plant to the tracks of the UP in order to enable UP to make coal deliveries directly to that plant. The establishment of dual rail access to the Drake plant is not economically and/or politically feasible due to the lack of sufficient land at the plant and surrounding the plant to permit the construction of the required additional rail line. In addition to including lower rail rates established through competition, the 2000 contract also included a unique rate adjustment formula crafted through mutual negotiations of the parties, among other provisions favorable to CSU.

In 2009 CSU approached UP to solicit a proposal for contract rates and service terms to replace the 2000 contract when it expired. In response, UP submitted a proposal that significantly increased the expiring contract rates. UP also demanded that a new contract include a fuel surcharge and rail car maintenance requirements over and above Association of American Railroad ("AAR") standards, which further raised the overall increase in costs to CSU. Moreover, UP submitted to CSU a "boilerplate" form contract which was very different from CSU's existing contract with UP. CSU also approached BNSF to solicit a proposal from it for delivering PRB coal to Nixon. However, BNSF demonstrated little interest in securing the 1,000,000 tons of annual PRB coal deliveries to Nixon. Specifically, BNSF declined to provide a contract proposal, and instead proposed to ship via a "pricing circular" which included rates and a fuel surcharge that together were over 300% of BNSF's estimated variable costs. CSU's renewed request for contract rates and service terms received no response from BNSF, and CSU eventually abandoned BNSF as an alternative for PRB coal transportation to Nixon in 2010, when its existing contract expired.

CSU was ultimately unable to agree to the terms and conditions of UP's contract proposal, and accordingly despite fully intending and desiring to enter into a new rail transportation contract or contracts in 2010, CSU presently ships all coal supplies of Drake and Nixon pursuant to common carrier rates established by UP which are over 30% higher than the expired contract rates, and pursuant to UP's coal common carrier service provisions.

5. <u>Other Factual Evidence Demonstrating a Present Lack of Effective Competition</u>

a. <u>Qualitative Data collected by Christensen Study</u>

The experiences of Utilities are not unique. For example, the Christensen Study involved the collection of "qualitative" and "quantitative" evidence on the state of competition in 2007 from shippers and other industry stakeholders. Chapter 5 of the study summarized the qualitative, anecdotal input the researchers received from rail shippers. Unfortunately, this input was then largely ignored in the study's quantitative analysis that followed,[15] but it included the following:

[15] Volume 2 of the Study contains the Study's "Analysis of Competition, Capacity and Service Quality," and states that it "presents our *quantitative* analyses and results" on competition in the railroad industry. Christensen Study at Vol. 2, 6-1. There is no comparable *qualitative* analysis of industry competition.

[s]ome shippers who had access to more than one railroad said that the advantages of having service from more than one railroad have diminished in recent years, *i.e.*, the competitive behavior of railroads has decreased.[16]

. . .[W]e heard that even when a shipper has access to two railroads, they cannot get the potential competitor to give them a bid against the incumbent railroad. This refusal to bid practice is viewed as an indication that the railroads are allocating markets among themselves. A variant on this view is the opinion expressed by some shippers that railroads don't seem to be hungry for new business.[17]

Much of the problem with service variability was attributed to reduction in rail competition. Moreover, since shippers stated that new contracts rarely include any performance standards or penalties for not meeting standards, so there is an increasing lack of railroad accountability.[18]

The Christensen Study stated that the "extensive stakeholder input greatly assisted in the focus of our research efforts and also indicated areas where further investigation is warranted."[19] However, the study ultimately drew conclusions as to the state of railroad competition based solely on quantitative economic formulas and assumptions.[20]

b. Service Quality and Cost Shifting

The decline of competition in the coal transportation sector has been marked in part by the elimination of measurable and enforceable railroad service standards in contracts, and the shifting of tasks and costs formerly performed and paid for by the Class

---

16 *Id.*

17 *Id.* at 5-11.

18 *Id.* at 5-12.

19 *Id.* at ES-4.

20 The Christensen Study did not attempt to reconcile or explain the differences and inconsistencies between the qualitative input obtained by shippers and the quantitative data, formulas and assumptions utilized to estimate railroad competition. In fact, the Christensen Study in places indicated it was not designed to analyze or reach conclusions about whether railroads were engaging in anti-competitive behavior in any particular market. Specifically, the Executive Summary contains the initial disclaimer that "[t]o address whether there has been an 'abuse of market power' would require judgments as to the fairness of the distribution of value between the railroads and the shippers . . . . These judgments are policy questions and not resolvable through economic analysis alone. Instead, we have answered the economic questions. . . ." *Id.* at ES-6.

I railroads to their shipper customers.[21] This shift has in recent years even occurred for dual-served shippers, which in the past were able to negotiate service standards and to reduce cost shifting attempts through competition between the railroads that could provide the service. Railroads have also unilaterally imposed rail car maintenance requirements on shippers which exceed the standards promulgated by the AAR. This is a form of cost shifting in that all the costs are borne by the shippers while any benefits are, at best, shared between the imposing railroad and shipper.

c. Lack of Rail Build-out Projects

Another indicator that effective competition for coal transportation service has substantially declined is that no shipper has sought authority from the STB to construct a line of rail for the purpose of creating dual rail access since 2003. Between 1990 and 2003, numerous parties, including utilities such as OPPD and CSU, sought to take advantage of the competition between the Class I railroads by incurring the sometimes substantial investment to construct rail tracks connecting their facilities to alternate railroads. As summarized above, OPPD clearly benefited from such efforts prior to 2008. Similarly, OG&E benefitted from the mere presence of a potential build-out in 1993. CSU also benefited from its build-out to UP in 2000. However, shippers have stopped seeking authority from the STB to construct tracks to create rail-to-rail competition, which is a strong indication that they doubt that such competition will occur and justify the significant costs of building out.

---

21 *See* Christensen Study at 5-12, 5-14.

d. **Fuel surcharges**

Consolidation of the rail industry has also resulted in the Board's Rail Cost Adjustment Factor being replaced by rate adjustment mechanisms that include rail "fuel surcharges." The assessment of such surcharges has been highly controversial, resulting in a decision issued by the STB in January, 2007 finding certain "fuel surcharge" practices to be unreasonable practices under 49 USC §10702.[22] In addition, a class action lawsuit is pending in the District Court of the District of Columbia accusing BNSF, UP, CSX and NS of conspiring to fix the price of rail services by colluding on fuel surcharge formulas that were designed to increase profits instead of recovering actual fuel costs.[23] *See also* STB Docket No. 42120, *Cargill Incorporated v BNSF Railway Company*, filed April 19, 2010, in which Cargill has filed a formal complaint challenging the reasonableness of BNSF's "mileage based" fuel surcharge. The Christensen Study nevertheless largely relegated railroad fuel surcharges to the category of "Future Research Direction," because it concluded STB data on fuel surcharges "have not been collected long enough at this point in time to perform a reasonable analysis."[24]

Utilities submit that the railroads' adoption and usage of their fuel surcharge formulas is further evidence that there is a lack of competition in the railroad industry. In a truly competitive environment in any industry, all other things being equal, the attempt by one competitor to assess a surcharge or fee that over recovered the costs it was trying to recoup would cause the loss of business to another company that established a

---

22 Ex Parte No. 681, *Rail Fuel Surcharges*, (served January 25, 2007).

23 Multi-district Litigation ("MDL") Docket No. 1869, *In re Rail Fuel Surcharge Antitrust Litigation* (class certification order pending).

24 *Id.* at ES-43; see also 5-21 ("the data are not sufficient to examine a number of issues related to these surcharges.")

surcharge that more closely tracked those costs. Yet all of the Class I railroads are still assessing fuel surcharges that are not being applied fairly and consistently, and which over-compensate them for their actual fuel costs for particular movements.

III. Policy Alternatives to Facilitate More Rail-to-Rail Competition

The consolidation of the railroad industry into essentially an oligopoly of two regional duopolies has clearly changed the competitive dynamics of the railroad industry and virtually eliminated effective rail-to-rail competition for the transportation of coal and other commodities.

The current state of the railroad industry poses difficulties when attempting to increase competition through the measures available to the STB, such as terminal trackage rights, reciprocal switching, and bottleneck segment relief. As one knowledgeable commenter has noted (as to reciprocal switching, but which is applicable to all forms of STB-granted competitive access relief) "[t]he experience with mandatory switching or short hauls to handoffs in Canada and Mexico has been somewhat disappointing, at least in part for a reason that is likely to restrict benefits in the United States as well: a competing duopolist fears that if it takes advantage of the opportunity to serve a shipper captive to its rival, the rival will in turn take advantage of the opportunity to serve its own captive shippers, and competition will break out throughout the system."[25]

Utilities assert that the diminished rail-to-rail competition in today's highly concentrated rail industry is certainly not the competition envisioned by Congress when it

---

[25] Pittman at 231.

enacted the Staggers Rail Act of 1980.[26] Accordingly, short of revisiting its approval of past major rail mergers and the conditions imposed on such mergers intended to preserve pre-merger competition, the Board should review its policies and rules concerning rail-to-rail competition with the goal of liberalizing those policies and rules to facilitate the resumption of effective competition between the Class I railroads, and competition between the Class I railroads and other non-Class I railroads. Suggestions include (1) modifying the so-called "Bottleneck Rules" to enable shippers to more easily obtain rates for segments of overall movements; (2) revising the Board's competitive access rules to facilitate the ability of additional railroads to compete to participate in rail movements; (3) confirming that physical access to a second railroad does not in and of itself mean that seeking rate relief from the Board is foreclosed; and (4) further revising the Board's rate reasonableness rules and policies.

A. **Revisions to the "Bottleneck Rules"**

The Board's so-called "Bottleneck Rules" resulted from the attempts by several electric utilities who were each captive at destination to a single Class I railroad to obtain common carrier rail rates over the segment of track owned by that railroad from the destination back to an interchange point between the bottleneck railroad and two or more other railroads who could provide service from a particular mine origin. Once the bottleneck rate was obtained, the shipper could then attempt to reap the benefits of competition between the railroads "above" the bottleneck and combine the winning rates and terms with the bottleneck rate, while preserving the ability to challenge the reasonableness of that rate at the STB. Absent a separately challengeable rate over the

[26] Pub.L. No. 96-448, 94 Stat. 1985.

bottleneck segment, the monopoly railroad could erase the benefits of any such competition and, if it served the origin, retain the overall business by pricing the overall through movement to protect its long haul. The underlying assumption in pursuing this rate strategy was that a total rate made up of (1) a rate arrived at through competition between multiple railroads from the mines to the interchange point, combined with (2) a maximum reasonable rate over the bottleneck segment, would be less than the overall maximum reasonable rate from origin to destination. In addition, pursuing a rate case over the bottleneck segment, if necessary, was expected to be less onerous and less expensive than challenging the entire rate from origin to destination. Finally, the threat of having to provide a bottleneck rate on request that could be challenged at the STB might have encouraged more reasonable contract rates and service terms from the monopoly railroad.

In a series of decisions issued in 1996 and 1997,[27] the Board rejected the utilities efforts and established the "Bottleneck Rules," which the Board generally summarized in its January 11 Decision in this proceeding.[28] Utilities strongly encourage the Board to revisit the Bottleneck Rules and revise them as necessary to facilitate the resumption of effective rail-to-rail competition. However, because of the reasons set forth above regarding the diminishment of rail-to-rail competition generally, and in their experiences specifically, Utilities believe that there are valid questions as to whether liberalizing the bottleneck rules to permit coal shippers to more easily obtain segmented rates would immediately result in overall rate levels from mine origins to captive destinations being

27 *Central Power & Light v. S. Pac., et al*, 1 STB 1059 (1996) ("*Bottleneck I*"); *clarified*, 2 STB 235 (1997) ("*Bottleneck II*"), *aff'd sub nom, Mid American Energy Co. v. STB*, 169 F.3d 1099 (8th Cir. 1999).

28 January 11 Decision at 3-4.

significantly reduced by vigorous competition between coal-hauling railroads.[29] Under such conditions, shippers gain little benefit from entering into a contract over the non-bottleneck portion of their routes and then requesting bottleneck rates, since the rates over the non-bottleneck segments are currently as high or higher than common carrier tariff rates and the service provisions are also similar. Nevertheless, the Board should take a hard look at the Bottleneck Rules and the authority relied upon to adopt them, and where possible modify the rules to maximize the opportunities for shippers to obtain separately challengeable segment rates.[30] Such modifications might facilitate the resumption of competition longer term by providing the short term possibility of rate relief over the bottleneck segment. The ability to more readily obtain rates over individual railroad segments would also better position coal shippers to gain from rail-to-rail competition where it can occur should meaningful rail-to-rail competition resume.

B. Facilitate the Ability of Additional Railroads to Participate in Rail Movements

The resumption of effective rail-to-rail competition for coal in the current transportation market could also be facilitated through the entry of additional participants into coal movements by expanding the scope of relief available under 49 U.S.C.

---

29 For example, that railroads would not "poach" on each others business and actively compete for contracts from mine origins to interchange points has been a concern of shippers since the "contract exception" was formulated by the STB in 1996. *See Bottleneck II* at 246-248.

30 As one example, the primary underlying authority for the Bottleneck Rules is *Great Northern Ry v. Sullivan*, 294 U.S. 458 (1935), a Supreme Court case involving joint line rail movements originating in Canada and terminating in the United States. In that case, the fact that the rail shipper negotiated and paid a single rate to one of the participating carriers, who paid a division to the other participating railroad, was a critical factor in the Court's decision. Such a rate is fundamentally different than movements separately billed to each participating railroad under so-called "Rule 11" movements, named for the applicable AAR Accounting Rule.

§10705(a)(alternative through routes), §11102(c)(reciprocal switching) and §11102(a)(terminal trackage rights). Each of these provisions, as written, generally include a broad "desirable and in the public interest" standard for relief. Indeed, in the case of §11102(c)(1), the statute states that the STB may require rail carriers to enter into reciprocal switching agreements "where it finds such agreements to be practicable and in the public interest, *or where such agreements are necessary to provide competitive rail service.*" (emphasis added). Nevertheless, the ICC twenty five years ago elected to construe these provisions very narrowly, establishing standards for relief so stringent that relief under these statutes is effectively precluded. These standards, embodied in the Board's regulations governing through routes under §10705 and reciprocal switching under §11102(c),[31] and ICC decisions starting with *MidTec Paper Corp. v. Chicago & NW Transp. Co*, 3 I.C.C.2d 171 (1986); *aff'd sub nom MidTec Paper Corp. v. United States*, 857 F.2d 487 (D.C. Cir. 1988)("*MidTec*"), make relief contingent upon a showing of "anticompetitive conduct" rising to the level of "competitive abuse." This requires the complaining party to "show that the incumbent railroad has used its market power to extract unreasonable terms or, because of its monopoly position, has disregarded the shippers needs by rendering inadequate service."[32]

---

[31] 40 CFR Part 1144. Requests for "terminal trackage rights" under §11102(a) are not covered by the Board's regulations, but the Board has nevertheless applied them in the few cases in which such rights have been sought. STB Docket No 41987, *Western Fuels Service Corporation v. Burlington Northern and Santa Fe Railway Company* (served July 28, 1997) at 7.

[32] January 11 Decision at 5, citing *MidTec* at 181. Cases involving coal transportation applying and/or discussing the "competitive abuse" standard include the Bottleneck Cases, *Western Fuels, supra*, and Docket NOR 42104, et al, *Entergy Arkansas, Inc. & Entergy Services, Inc. v. Union Pacific Railroad Company, et al*, (served March 15, 2011).

ICC and STB reconsideration of the extremely strict implementation of these statutory provisions has been unsuccessfully pursued by rail shippers for over two decades.[33] For example, the Board noted in 1998 that some rail shippers "as in the past" had argued that the *MidTec* standard "is too onerous, effectively precluding use of the competitive access remedy in an increasingly consolidated rail industry . . . ."[34] The uselessness of these rules has been exacerbated further still over the past decade as rail-to-rail competition has declined for coal and other commodities, even at plants that can be served directly by two railroads. In its decisions formulating the Bottleneck Rules, the Board articulated "an arguably more relaxed standard" than the competitive abuse standard for requests for new through routes under §10705.[35] This alternative "route efficiency" standard generally entails showing that an alternative routing is better or more efficient than the current routing.[36] While any movement away from the "competitive abuse" standard is a welcome change, the Board recently denied relief under §10705 in the one instance it has applied this standard.[37] The Board has stated its intention to "reconcile" the two standards "and more fully explore the legal framework to govern future competitive access cases" in this proceeding.[38] Utilities maintain that the current

---

33 *See, e.g.* STB *Ex Parte No. 575, Review of Rail Access and Competition Issues* (served April 17, 1998) at 6-7. In that proceeding, the STB noted shippers' complaints but responded by ordering the railroads to hold meetings with a broad range of shipper interests under the supervision of an ALJ to discuss potential revisions. These meetings produced no agreement on recommendations to the Board and no revisions were made. STB *Ex Parte No. 575, Review of Rail Access and Competition Issues* (served August 21, 1998).

34 *Id.*

35 Docket No. 42104, *Entergy Arkansas, Inc. et al v. Union Pacific Railroad Company, et al* (Decision served March 15, 2011) at 7-8; *citing Bottleneck I* at 1069.

36 *Id.* at 11-12.

37 *Id* at 16.

38 January 11 Decision at 8.

dearth of competition in the railroad industry requires that the Board take a very hard look at the *MidTec* "competitive abuse" standard, as well as the alternative "route efficiency" standard and, consistent with statutory language and legislative intent, modify them to more liberally permit the introduction of additional railroads into rail movements in order to foster rail-to-rail competition.[39]

C. Clarification of the Rules Governing Market Dominance at Locations With Access to Two Railroads

Shippers with access to another railroad would much prefer the resumption of meaningful rail-to-rail competition at their facilities, to pursuing rate reductions via a rate complaint at this Board. However, the significant rate increases and tariff-like contract terms imposed by the Class I railroads over the past few years have caused such shippers to consider taking such action. Such a case would immediately face the threshold issue of whether the Board had jurisdiction over the transportation at issue under the "qualitative" market dominance principles of 49 U.S.C. §10707 and agency decisions, since the defendant railroad would be expected to seek dismissal of the case on the grounds that the presence of another railroad alternative means there is indisuputably "effective competition" for the transportation at issue. Rail shippers such as OPPD, OG&E and CSU which have benefited from competition at their facilities in the past, but now are being assessed rates that might be found unreasonable under the Board's maximum rate standards, face particular uncertainty in this regard. As part of this proceeding, the Board should reaffirm that qualitative market dominance can be present in a concentrated market even if a shipper has access to two railroads, if it can be

---

[39] *See Greater Boston Television Corp. et al v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970) (agency may change course if it supplies a reasonable analysis).

demonstrated that if there is an absence of "effective competition" for the transportation to which a rate applies. Such a reaffirmation would be consistent with legislative intent, which was that market dominance could be found when rates exceed just and reasonable levels because of dupopoly behavior:

> Defining market dominance in terms of lack of effective competition avoids the problems of defining monopoly power which have arisen under the antitrust laws. Under this definition the publishing carrier need not have monopoly power. Rather the test will be whether the market itself is sufficiently competitive to insure just and reasonable rates. Thus, the Commission will be able to regulate maximum reasonable rates in oligopoly or concentrated markets as well as in monopoly markets. Lengthy antitrust-type litigation will be avoided by virtue of the Commission's authority to adopt rules of practical application which will identify markets in which dominance exists.[40]

Moreover, "while the absence of effective competition test is not intended to strictly conform with the standards of the antitrust laws, it is intended that when the Commission administers the test it will recognize the absence of forces which normally govern competitive markets."[41] The concept of "effective competition" was adopted in the Railroad Revitalization and Reform Act of 1976 (the 4-R Act)[42]. While the Staggers Rail Act later amended the 4-R Act and introduced the quantitative jurisdictional threshold prong of the market dominance test to 49 U.S.C. §10707, the Act did not substantively modify the qualitative prong adopted in the 4-R Act.

The ICC's development of rules to implement the market dominance concept reflected that a lack of effective competition could be found in duopoly railroad markets. For example, the ICC initially created several rebuttable presumptions for making a

40 S. Rep. 94-499, 94th Cong. 2d Sess. 1976 U.S.C.A.N. 14, 47 (emphasis supplied).

41 S. Conf. Rep No. 94-495, 94th Cong., 2d Sess. 1976 U.S.C.A.N. 147, 163

42 P.L. 94-210; 90 Stat 31 1976.

market dominance determination in a particular circumstance.[43] One of the presumptions was that market dominance was present if a carrier controlled more than 70 percent of the traffic at issue. However, the ICC also stated that "A shipper who is unable to demonstrate that the carrier controls over 70 percent of the traffic can prove market dominance by . . . presenting any other relevant evidence to show that there is an absence of effective competition. For example, a shipper could show that . . . carriers collusively share the market or follow parallel pricing policies to assure joint maximization of profits."[44] The original presumptions were replaced with general guidelines in STB Ex Parte No. 320, *Market Dominance Determinations and Consideration of Product Competition*, 365 I.C.C. 116 (1981). The ICC continued to define "effective competition" as consisting of pressure to lower rates or lose business. *See id.* at 129-30.

The significant concentration of the railroad industry into two regional duopolies for coal transportation raises serious questions of whether "effective competition," as envisioned by Congress, the ICC and the STB, still exists at certain locations where more than one railroad can provide, and in some cases have in the past provided, transportation services. While the resumption of meaningful competition at such locations would obviously be preferred to a regulatory solution, Utilities submit that providing clarity on the application of the Board's jurisdictional rules to such facilities in this proceeding would be beneficial.

---

43 Ex Parte No. 320, *Special Procedures for Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976*, 353 ICC 875 (Decided August 20, 1976).

44 *Id.* at 899 (emphasis supplied).

D. Modifications to Rail Rate Reasonableness Rules

While the Board has made strides in making its rate reasonableness procedures more accessible to rail shippers from a cost and process standpoint, Utilities submit that more changes to the Board's rules and procedures are necessary. For example, under the Staggers Rail Act, the Board's authority over rail rates is subject to a statutory floor of 180% of the railroad's variable cost of providing service. 49 U.S.C. §10707. Utilities are in favor of the Board's review of its Uniform Rail Costing System ("URCS"), since this outdated system, when combined with the 180% jurisdictional floor, produces very high minimum reasonable rate levels, particularly for efficient coal unit train movements. In addition, the Board should raise the damage limit of $5 million over five years in its Simplified Stand Alone Cost ("SSAC") rules. The Board's refusal to raise the limit was based in part on its conclusion that if potential damages exceed estimated litigation costs by only a small amount, then this is sufficient justification to bring a rate case under the applicable methodology, if the shipper believes it has a "strong" case.[45] But this conclusion fails to take into account factors such as the cost and harm of having to pay the challenged rate during the pendency of the case, and the general uncertainty inherent in any litigation, particularly a SSAC proceeding, for which there is no established precedent. Thus, for some utilities, even if they believe they have a "strong" case, the anticipated reparations and prescriptive rate relief may be insufficient under all the circumstances to justify the high cost of a full SAC case, yet such relief might exceed the $5 million SSAC threshold. Utilities submit that the Board should revisit its refusal to increase the $5 million damage limit for SSAC cases to $10 million. Increasing the

---

[45] STB Ex Parte No. 646 (Sub. No. 1) *Simplified Standards of Rail Rate Cases*, decision served March 19, 2008 at 7.

damage limit would shore up the regulatory backstop provided by the Board and provide a better means for mutually agreeable commercial resolutions to be negotiated.

IV. Modifying STB Policies to Increase Rail-to-Rail Competition will Not Negatively Affect the Viability of Class I Railroads

Modifying the STB's rules and policies to increase rail-to-rail competition by definition has an outcome of less regulation of railroads and more mutually acceptable commercial agreements. Nevertheless, the railroads consistently characterize any such efforts as "re-regulation" or increased regulation. The rote refrain from the Class I railroads when the possibility of revising STB policies to increase rail-to-rail competition is discussed is that to do so will stifle investment and threaten the long term viability of the railroad industry. For example, the AAR has consistently related to the STB and Congress that increased regulation will have a negative impact on railroads' ability to continue investments. As the AAR recently testified to the STB, railroads purportedly will be able to make investments only if the federal government maintains policies that allow "railroads and their investors to pursue returns on their enormous investments."[46] In the same testimony, the AAR emphasized that "changing the regulatory rules will lead to reduced investment and cost American jobs."[47]

The facts simply do not support this exaggerated response. Rather, multiple independent analyses and Wall Street judgments establish that the industry is financially healthy. Such data was recently collected and summarized in a September, 2010 report by the Office of Oversight and Investigations of the Senate Committee on Commerce, Science and Transportation ("Senate Report"), which concluded that Class I railroads'

---

[46] Comments of the Association of American Railroads, *STB Ex Parte No. 704, Review of Commodity, Boxcar, and TOFC/COFC Exemptions (January 31, 2011).*

[47] *Id.*

recent financial results show that "the Stagger's Act's goal of restoring financial stability to the U.S. rail system has been achieved" and that the Act "has produced a so-called 'rail renaissance.'"[48]

The overall finding of the Senate Report is supported by the Class I Railroads' Securities and Exchange Commission ("SEC") filings. These filings demonstrate that railroad companies in recent years have consistently gained solid revenues, and maintained stable or only slowly-growing expenses, even during the most recent economic downturn.[49] In fact, as emphasized in the Senate Report, in 2008 the railroad companies' profit margin placed the industry fifth out of fifty-three industries cited by Fortune as "most profitable."[50] Similarly, in 2010, the industry as a whole boasted record profits. In the last quarter of 2010 alone UP's, CSX's and NS's net income rose 41%, 42% and 31% respectively, and Berkshire Hathaway's profits went up 43% due to BNSF's contribution to earnings.[51]

The Class I railroads have continuously emphasized the need for capital investment and have maintained that their revenues do not allow them to address their

---

[48] Office of Oversight and Investigations of the Senate Committee on Commerce, Science and Transportation, *The Current Financial State of the Class I Freight Rail Industry*, p.1 (September 15, 2010).

[49] *Id.*, at 5.

[50] *Id.*, *citing* Fortune, *2008's Top Industries: Most profitable, Return on Revenues.*

[51] *See* Press Release, *Union Pacific Reports Record Fourth Quarter and Full Year,* (January 20, 2011), (online at *http://www.uprr.com/newsinfo/releases/financial/2011/0120_4qearnings.shtml*); The Wall Street Journal, *CSX 4Q Net Up 42% on Higher Volume; Results Top Street View* (online at *http://online.wsj.com/article/BT-CO-20110124-714302.html*); Press Release, *Norfolk Southern Reports 2010 Fourth-Quarter and Full Year Results* (January 25, 2011), (online at http://www.nscorp.com/nscportal/nscorp/Media/News%20Releases/2011/earn4q_10.html); The Wall Street Journal, *Berkshire Hathaway 4Q Net Income Up 43%* (online at http://onespot.wsj.com/business/2011/02/26/53724/berkshire-hathaways-4q-net-income-up-43).

long-term capital needs. The railroad industry is certainly capital intensive. However, the industry's assertions that revenues are insufficient to cover capital investment are plainly inaccurate. Specifically, according to the SEC filings submitted by the four largest Class I railroads (UP, BNSF, CSX, NS) over the past three years, those railroads spent approximately $25.7 billion in capital expenditures (roughly $8.9 billion in 2010, $7.8 billion in 2009 and $9 billion in 2008). On the other hand, these railroads also earned revenues totaling <u>$156.6 billion</u> in the same years (approximately $53.8 billion in 2010, $45 billion in 2009 and 57.8 billion in 2010). Thus, as noted in the Senate Report, "as the companies' revenues grew over the course of the decade, so did their capital investments."[52]

Other facts belie the notion that railroad revenues must be further increased to cover capital investment. For example, Class I railroads have been using their net income to increase their dividend payments. In 2010, with the overall economy still struggling to recover, UP twice announced dividend increases. The company's CEO commented, "as we generate strong and growing free cash flow, we are returning more cash to our shareholders...UP's strategy to operate a safe, productive, service-oriented railroad is delivering record results...for the year, the annual dividend increase totals 41 percent, reflecting both our confidence in the future and our commitment to increasing shareholders returns."[53] NS likewise increased its dividend by 6 percent last year[54] and,

---

52 Senate Report, *supra*, at 11.

53 Press Release, *Union Pacific Announces Second Dividend Increase in 2010* (November 18, 2010), (online at http://www.uprr.com/newsinfo/releases/financial/2010/1118_dividend.shtml).

54 Press Release, *Norfolk Southern Increases Dividend* (July 27, 2010), (online at http://www.nscorp.com/nscportal/nscorp/Media/News%20Releases/2010/div2q_10.html).

most recently in 2011, by 11 percent.[55] Similarly, in 2010, CSX increased its dividend by 8 percent, which marked CSX's eighth increase during the past five years.[56]

Net income was also used by railroads to repurchase their publicly-traded shares to attain short-term gains in stock value. The four major U.S. railroads spent over $2 billion in share buybacks in 2006, over $6 billion in 2007, and over $5 billion in 2008. Although these companies halted share buybacks in 2009, they resumed their repurchase practices in 2010.[57] As the Senate Report notes, the capital expended to buy back shares and attain short-term gains was spent "at the expense of investments that increase capacity and productivity."[58]

Finally, despite statements from the AAR that Wall Street investors are "increasingly skittish about the tone in Washington D.C,"[59] Wall Street retains its bullish view of the Class I railroads. The quantitative stock report published by Standard & Poor in September of 2010 gave quality rankings of "A", "A-" and "B+" to Union Pacific, Norfolk Southern, and CSX, respectively. Union Pacific and Norfolk Southern scored above the 90th percentile on S&P's "Investability Quotient", and CSX received a score of 89%, which further confirms the continued attraction of investment in the industry.[60]

---

55 Press Release, *Norfolk Southern Increases Dividend* (January 25, 2011), (online at http://www.nscorp.com/nscportal/nscorp/Media/News%20Releases/2011/4q_2010_dividend_increase.html).

56 Press Release, *CSX Corporation Announces Dividend Increase* (September 29, 2010), (online at http://www.csx.com/index.cfm/media/press-releases/csx-corporation-announces-dividend-increase/).

57 Senate Report, *supra*, at 12-13.

58 *Id.*, at 12.

59 Mitchell, *supra*.

60 Senate Report, *supra*, at 6-7.

V. <u>Conclusion</u>

The utilities submitting these Joint Initial Comments commend the Board for holding this timely proceeding to receive information on the state of competition in the railroad industry, and on possible changes to the Board's existing rules and policies concerning rail-to-rail competition. The significant consolidation of the railroad industry in the United States into essentially two regional duopolies has resulted in the significant reduction of competition between the Class I railroads for many coal shippers, including coal shippers who have access to more than one railroad for service. The current concentrated rail market requires that the Board commence a formal review of its rules policies concerning rail-to-rail competition and related rules such as rate reasonableness standards. Such rules and policies should be modified to encourage the resumption of meaningful rail-to-rail competition, while also meeting the Board's other statutory responsibility of ensuring a viable railroad industry in the United States.

Respectfully submitted

Thomas W. Wilcox

Thomas W. Wilcox
Svetlana Lyubchenko
GKG Law, P.C.
1054 Thirty-First Street, NW, Suite 200
Washington, DC 20007
(202)342-5248

Counsel for Omaha Public Power District; The AES Corporation; Oklahoma Gas & Electric Co.; and Colorado Springs Utilities

PRESS CLIPS JULY 17, 1998

OPPD
Omaha Public Power District

Omaha World-Herald, July 17, 1998

OPPD Track Buy Saves $60 Million on Rail Contract

BY PATRICK STRAWBRIDGE
WORLD-HERALD STAFF WRITER

It didn't take long for the Omaha Public Power District board to start spending — and saving — money Thursday night.

Board members approved contracts for more than $10 million in construction and renovation projects in the first 20 minutes of their monthly meeting. Then they passed the biggest expenditure of them all — a five-year contract package worth $265 million for coal supply and rail transportation.

That deal, OPPD officials said, will save the district more than $60 million over the next five years. Board member Keith Edquist alluded to the benefit of saving that money.

"I think this is where we get our money for all the stuff we just bought," he said as the board prepared to vote on the coal and rail contracts.

The board met at its Energy Plaza headquarters in downtown Omaha.

Coal and rail costs are among the utility's largest expenses. They represent at least 16 percent of OPPD's annual operation and maintenance budget.

The current rail contract, which is with Burlington Northern Santa Fe, is for $222.3 million, OPPD spokesman Gary Williams said.

Burlington Northern did not face competition for a key part of past coal transport contracts because it owned the only track leading from Lincoln to OPPD's coal-fired power plant in Nebraska City, Neb. But OPPD's recent purchase of that 57-mile stretch of track made competitive bids possible.

The contract is the product of several years' work. On Tuesday, the board met in a marathon closed session that OPPD President Fred Petersen said was the lengthiest he could recall in his 30 years with the district.

"They questioned us and challenged us as much as we've ever been challenged," Petersen said. "I'm not saying that's a bad thing."

One tough decision was the choice of Burlington Northern over hometown railroad Union Pacific, said board member John Green. The U.P. bid was more than $2 million higher than Burlington Northern's $160.8 million offer, he said.

"We've had a long history of buying Omaha," Green said. "That is something very significant and important to everyone here. But I have to say, the money is just too significant a benefit for the ratepayers."

Board member Michael Cavanaugh agreed.

"The decision we face tonight is very tough," he said. "But whichever route we take, the ratepayer will benefit."

The rest of the $265.7 million package gives the coal supply contract to Arch Coal Sales Co., the rail line maintenance contract to Kelly-Hill Co. and the rail line operator contract to Kyle Railroad Co.

The board also approved:

- $5.8 million for construction and improvements to the OPPD substations in Blair, Omaha, at the Cargill facility in Washington County and near the Fort Calhoun power plant.
- $2.3 million for transmission-line projects running from the Fort Calhoun Power Station to one in Blair, and from there to one near 204th and Pacific Streets.
- A $15 million reduction in 1998 funding for the decommissioning fund for the Fort Calhoun station. A recent study showed that the additional funding was unnecessary.
- $395,400 for improvements to the Elkhorn Service Center, including a new storage building.

Exhibit 2

7/16/03

OPPD switching to U.P. in new 5-year contract

BY NANCY GAARDER
WORLD-HERALD STAFF WRITER

In a significant decision in terms of fuel and expense, the Omaha Public Power District is planning to switch rail and coal companies for its next five-year contract.

In January, for the first time since 1984, Union Pacific Railroad is expected to haul coal to OPPD's power plants. Bids analyzed recently indicate that a coal-rail package using Union Pacific is about 6 percent lower, or $15 million less, than one using the Burlington Northern and Santa Fe Railway.

Burlington Northern has been transporting coal to OPPD's north Omaha plant since 1984 and to the utility's Nebraska City plant since 1978.

The OPPD board will vote Thursday on the Union Pacific coal-rail bid package, which is valued at $245.7 million. The Burlington Northern package is $260.5 million.

Coal is OPPD's main source of fuel, supplying about two-thirds of the utility's fuel last year.

Dale Widoe, vice president at OPPD, said the cost of the new contract package is about 3 percent above an inflation-adjusted value of the current contract. Describing that as a "very modest" increase, Widoe said the contract is an important part of keeping electric rates low.

"With U.S. energy costs going up rapidly," Widoe said, "the coal contracts introduce real stability into our rate-making."

Widoe said the fuel package should have a "negligible" effect on electric rates. OPPD's 3.1 percent increase in rates that goes into effect in January is due not to the coal contract, Widoe said, but to the utility's need to spend about $1 billion retooling and expanding its electric plants.

See OPPD: Page 2

OPPD: U.P. gets coal contract

Continued from Page 1

Given that Union Pacific has its headquarters in Omaha, board member John Green was happy to see the rail portion of the contract come home.

"This is 'buy Omaha' at its best," Green said.

Burlington Northern is based in Fort Worth, Texas.

OPPD has been working on the contracts since the fall and has been briefing the board since February. Board member Kirk Brumbaugh Tuesday praised the board for its careful work.

"This was done objectively with no political influence or favoritism shown on the part of the board or management," he said.

Putting together each bid package was a bit like a jigsaw puzzle. Eleven companies bid on the coal contracts, 15 on short-line rail operations, five on rail-line maintenance and two, Union Pacific and Burlington Northern, on long-distance transportation.

In compiling the packages, OPPD had to weigh coal costs against transportation and other costs.

For example, Burlington Northern has access to all the coal mines in Wyoming, which meant that if OPPD had selected Burlington Northern, it could have picked from a larger number of coal bids. Union Pacific can reach only the southern mines.

On the other hand, Union Pacific has direct access to OPPD's two coal plants, which can favorably affect the amount it can charge. To reach OPPD's north Omaha plant, Burlington Northern would have to travel along a five-mile piece of Union Pacific tracks, something that Union Pacific charges for. To reach the Nebraska City plant, Burlington Northern would have to use OPPD's tracks from Lincoln and pay a short-line hauler to move the coal.

Coal and transportation each account for about half the total package, Widoe said, with a small slice going to rail maintenance.

The coal comes from some 670 miles away in Wyoming's Powder River Basin. Because the coal has a low sulfur content, Widoe said, it generates fewer problems in terms of air emissions.

The coal contract includes a combination of fixed and market prices, Widoe said. Because Union Pacific can't reach all the coal mines, OPPD will have less flexibility in responding to fluctuating coal prices. That "loss of opportunity" was factored into the bid analysis, Widoe said.

The winning coal bid came from Kennecott Energy Company. The current coal contract is with Arch Coal. CANAC Yard Services will provide railway maintenance.

Representatives from Union Pacific and Burlington Northern had no comment on the bids.

Exhibit 3

Expect to get jolt from electric bill

Rising costs prompt OPPD to propose its biggest rate increase since 1973.

By Steve Jordon
WORLD-HERALD STAFF WRITER

Starting Jan. 1, Omahans likely will get their biggest electricity rate increase in 35 years.

The increased costs of coal and of hauling it from Wyoming to Nebraska are behind a plan to raise average electrical bills for homeowners by 11 percent and for businesses as much as 27 percent, with the overall average 14.6 percent.

OPPD's last rate increase above 10 percent was in 1973, a time when the nation also was struggling with energy costs.

"This isn't something we enjoy doing," said W. Gary Gates, OPPD's president and chief executive, this morning. "But we

See OPPD: Page 2

OPPD rates rising

Impact of proposed rates on average monthly bills.

	Current	Proposed	Increase
Residential	$79.49	$88.22	11.0%
Small business	$97.37	$110.93	13.9%
Medium business	$1,724.17	$1,978.37	14.7%
Large business	$27,974.18	$33,217.58	18.7%
Industrial	$312,164.92	$396,906.19	[illegible]
Towns	$54,276.29	$63,740.23	17.4%
Overall percent increase			14.6%

Comparison of proposed rates, cents per kilowatt hour

	OPPD	Region	Difference	National	Difference
Residential	8.61	9.40	-8%	12.30	-30%
All customers	6.71	7.80	-14%	10.60	-37%

SOURCE: Omaha Public Power District

DEAN WEINLAUB/THE WORLD-HERALD

OPPD: Coal, transportation costs up

Continued from Page 1

feel it's important to share this information."

In November the public utility's managers will recommend the rate increases to its elected board, which is expected to vote on the proposal Dec. 11.

If approved, the "fuel and transportation cost adjustment" would appear as a new separate line on customers' bills.

Fred J. Ulrich, chairman of OPPD's publicly elected board of directors, said the increase appears unavoidable. "Right now this looks like the only option."

He said OPPD and its managers worked hard to offset other cost increases, such as medical expenses and damage from recent storms, and wouldn't have proposed a rate increase but for the sharply higher coal and transportation costs.

The increase, affecting customers in 13 counties, would add nearly 1 cent per kilowatt hour of electricity. Since the average home uses about 1,000 kilowatt hours per month, the average monthly bill would go up $8.73.

Gates said OPPD's rates would remain below the Midwestern average. Other utilities in the region also are raising rates or will raise rates as they negotiate new coal and transportation contracts, he said.

All utilities are facing "dramatic and unprecedented" increases in costs for coal and transportation, he said.

Kansas City Power and Light, for example, last week said it wants to raise rates by an average of 17.5 percent.

Earlier this year OPPD negotiated five-year contracts for coal supply and rail transportation, with Union Pacific Railroad beating out Burlington Northern Santa Fe for the rail contract.

The lowest bids were for $107 million more per year for 2009 than in 2008. OPPD trimmed that increase to about $97 million.

The new coal and transportation contracts were 150 percent higher than the existing contracts, which expire at the end of this year. The cost-cutting reduced that increase to about 135 percent, Gates said.

OPPD reduced costs by buying lighter, fuel-saving aluminum railcars and by purchasing coal on the spot market at lower prices.

"We're going to continue to make whatever belt-tightening we can here at OPPD," Gates said. "But the amounts are so large that we can't absorb that within our current budgets."

Gates said coal and transportation make up 15 percent of the cost of electricity, but that percentage will rise to 25 percent next year under the new contracts.

Diesel fuel is one factor and increased demand for coal is another. U.S. utilities from as far away as Atlanta are using Wyoming coal, he said.

OPPD's new contracts allow for lower rates if the price of fuel drops below 2003 levels, Gates said, but that doesn't seem likely.

"I wouldn't want to give a false sense that we are going to see a big improvement," he said. "We'd lock this in for at least a one-year period," and the increase might be permanent.

Residential and commercial customers have said they want stable electricity prices so they can plan their budgets, he said. That's why OPPD is announcing the proposed increase now.

OPPD said switching to solar or wind power wouldn't cut costs because those energy sources are more expensive than coal-generated power.

Replacing the new Nebraska City power station with wind turbines would cost at least $25 million a year more, even counting the higher coal and transportation costs, OPPD said, and would not provide full-time power because of variable winds.

OPPD said it plans to increase the generating capacity of its Fort Calhoun Nuclear Station, but the utility is too small to take on the cost of building a new nuclear plant by itself.

Such a plant may be possible in the future, OPPD said.

Contact the writer:
444-1080, steve.jordon@owh.com